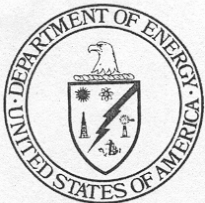




U.S. Department of Energy
Office of Inspector General

Special Report

Los Alamos National Laboratory's
Purchase Card Program Corrective
Actions




Department of Energy

Washington, DC 20585

April 12, 2004

MEMORANDUM FOR THE SECRETARY

FROM:


Gregory H. Friedman
Inspector General

SUBJECT:

INFORMATION: Special Report on "Los Alamos National Laboratory's Purchase Card Program Corrective Actions"

BACKGROUND

The University of California operates the Los Alamos National Laboratory (Laboratory) for the Department of Energy's National Nuclear Security Administration (NNSA). Among its many vital missions, the Laboratory ensures the safety, security, and reliability of the nation's nuclear weapons stockpile. To carry out its various missions, the Laboratory spends nearly \$2 billion annually in Federal funds of which approximately \$15 million is expended on low cost items using purchase cards. The use of purchase cards permits Laboratory employees to make small purchases in an efficient and timely manner. While convenient, programs of this type and scale are inherently vulnerable to misuse and thus require close and continuing management attention to protect against potentially fraudulent or abusive purchases.

In late 2002, the Laboratory was the subject of intense scrutiny as a number of questionable purchase card transactions came to light. Subsequently, University of California-chartered External Review Committee, Congressional, and Office of Inspector General reviews disclosed a number of weaknesses in the Laboratory's purchase card program. In particular, an Office of Inspector General Special Inquiry on *Operations at the Los Alamos National Laboratory*, (DOE/IG-0584, January 2003) and an Interim Inspection Report on *Internal Controls over Personal Computers at Los Alamos National Laboratory*, (DOE/IG-0597, April 2003) pointed out a number of procurement and property related weaknesses. In several forums, including Congressional hearings, officials from the University committed to correcting deficiencies in the Laboratory purchase card system. Because of the significance of the issues disclosed through prior examinations, we performed a follow-up review to determine whether the Laboratory had conducted a thorough analysis of its purchase card program and had initiated corrective action to resolve previously reported weaknesses.

RESULTS OF REVIEW

Our follow-up review found that the Los Alamos National Laboratory had significantly improved the management of its purchase card program. Our detailed review of over 600 transactions spanning a 5-year period – covering periods both before, during and after the



turbulence in 2002 and 2003 – and an automated analysis of about 60,000 transactions completed in Fiscal Year 2003 revealed that the Laboratory had implemented numerous corrective actions in response to recommendations made by the Office of Inspector General and other review teams. We also noted that the environment at the Laboratory appeared to reflect a commitment to improve its purchase card system. Many positive steps had already been implemented. For example:

- The number of active purchase cards had been reduced from about 800 to 550;
- Purchase card transactions were subjected to multiple reviews and electronically reconciled to supporting documents;
- Cardholders were no longer allowed to approve their own transactions; and,
- Approving officials were responsible for fewer purchase cardholders, permitting them to provide additional scrutiny of transactions.

Clearly, the progress to date had been substantial. During our review, however, we identified certain opportunities to further reduce the risk of purchase card misuse at the Laboratory. For example, the Laboratory could: (i) enhance guidance to purchase cardholders by clarifying the rationale for items that should not be acquired by purchase card and the processes for seeking exceptions to those restrictions; (ii) automate its data analysis techniques to identify purchases that do not comply with internal guidance; and, (iii) enhance its periodic reviews of cardholder activities by improving follow-up actions to correct noted problems and consistently imposing sanctions for departures from established procedures. The report includes recommendations to assist the Department in this regard.

During this review, we confirmed the findings of other reviewers and assessed the adequacy of the Laboratory's corrective actions in response to those reviews. To achieve this goal, we interviewed Laboratory and NNSA officials, reviewed relevant purchase card documents, and tested a wide range of randomly and judgmentally-selected purchase card transactions. Separately, the Office of Inspector General is currently evaluating the adequacy of internal controls at the Laboratory for certain categories of personal computers.

We are issuing a separate internal report to management that provides specific details on a single purchase cardholder that, due to Privacy Act considerations, could not be included in this public report.

MANAGEMENT REACTION

NNSA agreed with the report and recommendations and indicated that the Laboratory had implemented or initiated corrective action.

Attachment

cc: Deputy Secretary
Administrator, National Nuclear Security Administration
Manager, Los Alamos Site Office

REPORT ON LOS ALAMOS NATIONAL LABORATORY'S PURCHASE CARD PROGRAM CORRECTIVE ACTIONS

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Background

As a result of a series of reviews that began in August 2002, numerous recommendations were made to strengthen controls over Los Alamos National Laboratory's purchase card program. One of these reviews, conducted by an External Review Committee (Committee),¹ chartered by the University of California (University), examined Laboratory purchase card transactions and related controls. The Committee's conclusion was that weaknesses in the program left the Laboratory "vulnerable to fraud and abuse." The Committee made a series of recommendations designed to strengthen the program in its report and also provided the Laboratory with 5 lists containing over 8,400 transactions that required additional review and disposition. Subsequently, the Laboratory performed an internal review of the transactions and made a preliminary determination as to their disposition. This internal review process was then subjected to an examination by the University's chief auditor.

In addition, the Laboratory's Associate Director of Administration issued a memorandum in August 2002 that recognized that purchase card controls needed to be improved and spending limits were excessive. Laboratory officials also accepted most of the recommendations made by various review groups and committed to take needed corrective action. Prior to initiating our review, the Laboratory reported that it had taken corrective actions to address the concerns raised by the prior reviews.

Prior Reviews of the Laboratory's Purchase Card Program

Based on an examination of the work performed by the Committee, we determined that the review was comprehensive and could be relied upon. Our conclusion was based on an examination of the draft report, reviews of the working papers on which the report was based, and interviews of key members of the review team that supported the Committee's efforts. With a minor exception, we arrived at the same conclusions as the Committee.

Our test work also indicated that the Laboratory had adequately addressed the 8,400 transactions identified by the Committee for further review. We tested a sample of the items analyzed by the Laboratory to confirm its assertion that the transactions had been reconciled to supporting documentation and determined to be allowable, or were in the process of being reimbursed to the Department. We arrived at the same conclusion as the Laboratory for these transactions.

¹The External Review Committee was comprised of two independent experts, supplemented by forensic accounting services provided by the public accounting firm of PricewaterhouseCoopers.

Response to Previous Recommendations

Using automated analytical tools, and with selected testing of specific transactions, we independently reviewed 60,000 Fiscal Year (FY) 2003 purchase card transactions. We determined that the Laboratory, among other corrective actions, had implemented the improvements described below:

- Purchase card transactions were subjected to multiple reviews. The reconciliation process required that an approving official review each transaction and that a group manager approve a monthly "Stewardship Report" detailing all purchase card transactions for that group. The Laboratory's Purchase Card Office also manually scanned all purchase card transactions each month looking for unusual items. Finally, over 100 purchase cardholders were randomly selected every quarter, and the Purchase Card Office reviewed 100 percent of their transactions.
- Purchase card transactions were electronically reconciled to supporting documentation, and manual reconciliations were no longer allowed. In addition, the Purchase Card Office issued sanctions to cardholders that had not completed the reconciliations in a timely manner.
- Cardholders were no longer allowed to approve their own transactions regardless of their procurement authority.
- Inappropriate merchant category codes had been blocked by the servicing financial institution to prevent transactions with certain vendors.
- A "business purpose" field was added to the purchase card system and we found that it was accurately populated.
- Spending limits were reduced, and approving officials were responsible for fewer purchase cardholders, permitting them to provide additional scrutiny of transactions.
- The Laboratory's purchase card training program was updated and provided to all cardholders and approving officials. Training included information on types of items not authorized for purchase, requirements for supporting documentation, and safeguards for purchase cards. We further noted that purchase card privileges had been suspended for cardholders and approvers who failed to attend the training.

Remaining Corrective Actions

While we observed that the vast majority of corrective actions had been appropriately addressed by the Laboratory, we noted a few areas in which controls implemented to correct previously reported weaknesses could have benefited from additional action or follow-up. For example:

- While both the University and the Laboratory drafted and disseminated purchase card policies, policies for the Purchase Card Office had not been finalized and officially adopted as of the date of our review.
- The sanction process for violations had not been consistently implemented. We found that sanctions had not been issued for violations occurring during a three-month period in FY 2003. Further, when sanctions were imposed on approving officials for violating purchase card policies, their supervisors were not always notified.
- Although information was collected and tracked on violations of purchase card controls, analyses were not performed to identify trends in repeat offenders or categories of violations.

Enhancing controls in these areas should compliment safeguards at the Laboratory, improve efficiency, and help ensure that inappropriate purchases are prevented or detected in a timely manner.

Further Opportunities To Enhance Controls

While progress at the Laboratory was noteworthy, we identified certain opportunities, not specifically covered by previous recommendations, to further enhance controls over the Laboratory's purchase card program. Specifically, we noted that clarification of restrictions on purchasing certain items, the use of automated transaction review techniques, and strengthening periodic reviews could further reduce the risk associated with the Laboratory's purchase card program.

Use of Unauthorized Items List

The Laboratory maintained an "Unauthorized Items List" to help ensure that items management considers to be inappropriate were not acquired with purchase cards. While the list covers a wide range of items, the Laboratory had not delineated the reasons for placing an item on the list or the procedures to be employed when seeking or granting an exception. Based on our review, we concluded that including such clarifications would assist cardholders in determining the propriety of acquisitions. In

particular, we determined that such enhancements could help cardholders avoid purchases similar to the 16 questionable transactions identified during our testing. For example, we noted that items such as a mini utility-vehicle, chemicals, food, and certain electronic equipment were acquired even though they appeared on the list of unauthorized items. While Laboratory officials told us that many of the items we identified were based on approved exceptions and had valid business purposes, we noted that the purchases were inconsistent with guidance in effect at the time of the acquisition and evidence of waivers was not provided.

Automated Review Techniques

The Laboratory could also increase the effectiveness of its periodic review of purchase card transactions by using automated techniques such as those utilized during our review. The Purchase Card Administrator was required to examine a large volume of transactions using manual methods – a technique that increased the likelihood of overlooking exceptions. In contrast, we used data analysis software to test over 60,000 FY 2003 purchase card transactions. This effort identified 58 transactions that may have been split to avoid purchase card limits that were not noted during the Laboratory's own periodic reviews. Daily or dollar value limits are particularly important because they reduce the risk associated with high value purchases and help to ensure that high volume purchases are based on other, possibly more efficient, negotiated instruments. Of the 20 items we specifically tested, 8 involved multiple transactions that could have been charged as a single transaction. Absent a compelling justification, split purchases are an unacceptable practice.

In the particular examples we identified, management acknowledged that a few transactions were split to avoid purchase limits. Laboratory officials told us that they had not previously focused on identifying transactions of this type and agreed that using automated techniques could increase the efficiency of their reviews. The use of such techniques would not only help identify split purchases but have the potential to speed the review for unauthorized items as well. Laboratory officials indicated that they planned to procure an enhanced version of the same data analysis software used during our review.

Periodic Review Follow-up

Finally, to verify that cardholders are complying with internal guidance, the Laboratory subjects transactions to multiple monthly reviews, with certain individuals randomly selected for more detailed quarterly audits. Monthly reviews are limited to reviewing information describing vendor, item description, and cost. Quarterly audits are more detailed and include the additional step of reviewing supporting documentation. If problems are identified, the Laboratory takes actions such as sanctioning the cardholder, including suspending or canceling purchase card privileges. We noted, however, the only action taken when problems of insufficient documentation were identified during quarterly reviews was to schedule a follow-up audit for the next quarter. The effectiveness of the periodic review program could be improved by requiring that follow-up actions are initiated to remedy or correct problems discovered.

RECOMMENDATIONS

To provide additional assurance that the Laboratory's purchase card program is operating as intended, we recommend that the Los Alamos Site Office Manager direct the Laboratory to:

1. Revise existing purchase card policies including clarification of the Unauthorized Items List and finalize and formally adopt policies governing the Purchase Card Office;
2. Complete the acquisition of data analysis software and verify that it is being appropriately used to review purchase card transactions;
3. Ensure that all violations are accompanied by an appropriate sanction and that supervisors are informed of all violations;
4. Require follow-up and resolution of specific transactions identified by internal reviews as unsupported or not in accordance with Laboratory policy; and,
5. Revisit corrective or follow-up actions noted in this report requiring additional action, including trend analyses.

MANAGEMENT REACTION

Management agreed with the finding and recommendations and indicated that corrective actions were in process or completed. Management's verbatim comments are included in the appendix to this report.

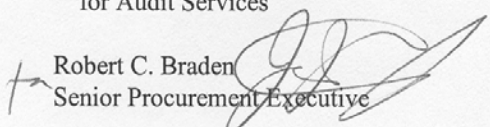


Department of Energy
National Nuclear Security Administration
Washington, DC 20585



APR 08 2004

MEMORANDUM FOR William S. Maharay
Deputy Inspector General
for Audit Services

FROM: Robert C. Braden 
Senior Procurement Executive

SUBJECT: Comments on IG's Draft Report on LANL's
Purchase Card Program

The National Nuclear Security Administration (NNSA) appreciates the opportunity to have reviewed the draft Special Report, "Los Alamos National Laboratory's Purchase Card Program Corrective Actions." We understand that the objective of the review was to determine whether the Laboratory had conducted a thorough analysis of its purchase card program and had initiated corrective actions to resolve previously reported weaknesses. NNSA agrees with the report and the specific recommendations.

We appreciate the IG noting that the environment at the Laboratory appeared to reflect a commitment to improve its purchase card system. The Laboratory has made significant strides in strengthening their Internal Controls program and specifically has improved the management of its purchase card program, as evidenced by the report. The Laboratory has implemented, or is in the process of implementing, corrective actions to the recommendations made in this report. In fact, the revision to Desktop procedures is 85% complete and will be completed in June; acquisition of the data analysis software should be completed in October; the recommendations related to violations and auditing processes have been completed; and trending analysis will begin in July.

Should you have any questions related to this response, please contact Richard Speidel, Director, Policy and Internal Controls Management. He may be contacted at 202-586-5009.

cc: Michael Kane, Associate Administrator
for Management and Administration
Ralph Erickson, Manager, Los Alamos Site Office

**Comments to
Inspector General's Draft Special Report
"Los Alamos National Laboratory's
Purchase Card Program Corrective Actions"**

RECOMMENDATIONS

"To provide additional assurance that the Laboratory's purchase card program is operating as intended, we recommend that the Los Alamos Site Office Manager direct the Laboratory to . . ."

Recommendation 1

Revise existing purchase card policies including clarification of the Unauthorized Items List and finalize and formally adopt policies governing the Purchase Card Office.

Management Comment

Concur

Cardholder procedures have been revised to clarify the reason for placing items on the Unauthorized Items List and how exceptions may be obtained. Desktop procedures are approximately 85% complete. Estimated completion date for this recommendation is June 2004.

Recommendation 2

Complete the acquisition of data analysis software and verify that it is being appropriately used to review purchase card transactions.

Management Comment

Concur

The Los Alamos National Laboratory is currently in the process of acquiring software to perform data analysis. The estimated completion date to acquire the software and commence data analysis is October 2004.

Recommendation 3

Ensure that all violations are accompanied by an appropriate sanction and that supervisors are informed of all violations.

Management Comment

Concur

Appendix (continued)

The Laboratory has revised the cardholder procedures to include a policy related to sanctions. Additionally, supervisors are now notified whenever a violation occurs. Actions for this recommendation have been completed.

Recommendation 4

Require follow-up and resolution of specific transactions identified by internal reviews as unsupported or not in accordance with Laboratory policy.

Management Comment

Concur

The Laboratory has modified their internal auditing procedures to capture the requirement to conduct follow-up reviews to ensure resolution of identified problems or issues. Actions for this recommendation have been completed.

Recommendation 5

Revisit corrective or follow-up actions noted in this report requiring additional action, including trend analysis.

Management Comment

Concur

In addition to follow-up analysis, the Laboratory will conduct trend analysis on a semiannual basis commencing in July 2004.

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